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SUBJECT: OUTLOOK FOR THE EU'S THIRD ENERGY PACKAGE

¶1. (SBU) Summary. EU Commission officials tell Econ Officers that the French Presidency plans to defer action on the Third Energy Package this year, with the package to be acted on by the Czech Presidency after the first of the year.

There are large differences between the current Council and Parliament versions of the package, but Commission, Council, and Parliament officials are optimistic that a political agreement can be reached next Spring before the Parliament begins its election cycle. End Summary.

¶2. (SBU) Econ Officers met October 30 with Ana Arana Anelo, Head of Unit for Electricity and Gas in DG-TREN to discuss the status of the EU's Third Energy Package. Arana confirmed that the French Presidency has decided not to schedule this package for this year and instead will pass it to the Czech Presidency next Spring. Arana indicated that, while the Commission does not necessarily agree with all the changes approved by the October European Council, the essential elements of the package are still intact. She believes that, even though the Council has watered down the requirements for ownership unbundling, the version proposed by the Council will still accomplish the goal of bringing greater competition to the internal market for gas and electricity and encouraging interconnection of the grids between member states. Arana was confident that the package could be presented to the Parliament early next year with adequate time for consideration and approval before the Parliament recesses for elections.

The Council Version

¶3. (SBU) On October 10 the Energy Council reached formal agreement on the third Internal Energy Market Package. Although the previous Energy Council in June had agreed to the Internal Energy Market package in principle, there remained some issues to discuss in detail, and the text to finalize, in particular the "third country clause" and "level playing field" clause. The October 10 Energy Council resolved these issues as follows:

-- The third country clause requires Member States, through national regulators, to undertake a specific procedure to determine whether a potential acquisition of an electricity or gas network in the EU by a company from a third country fully complies with the EU's rules on unbundling and whether it potentially provides a threat to that countries' and the EU's security of energy supply. In the event that it concludes that it does, it may prohibit that acquisition. The decision of the Member State must be referred to the Commission, which gives an opinion whether the acquisition meets the unbundling requirements of the Directive and/or represents a threat to the EU's security of energy supplies. The Member State must take the "utmost account" of the Commission's view, which is not however binding.

-- The level playing field clause imposes restrictions on vertically integrated companies from one Member State from buying unbundled energy companies in another. The Council

agreed to a clause that makes it clear that member states can legally prevent vertically integrated companies (i.e. companies owning generation, supply and transmission) from purchasing their ownership unbundled transmission grids. Furthermore Member States can also prevent such companies from purchasing their generation/supply companies on grounds of overriding public interest.

¶4. (SBU) The other elements of the package were approved as per the agreement of the Council of June 6th. In particular it permits Member States to choose between ownership unbundling and the Independent Transmission Operator (ITO) model. The ITO model accepts that a company may remain vertically integrated, and in many respects seems to be based on, but then expands on, a proposal tabled earlier by the eight Member States opposed to ownership unbundling. In addition, the idea of having an independent trustee that would be responsible for appointing the supervisory board was dropped. An agreement has also been reached on the establishment of a new Agency for European Energy Regulators, a new transmission system operator (TSO) body with a more formal role, a new procedure for adopting common network rules, and common minimum powers and levels of independence for national regulators.

Where the Differences Lie

¶5. (SBU) The next step will be negotiations between the Council and Parliament.

-- The Parliament in its First Reading adopted an opinion which only allows ownership unbundling for electricity, and the choice between ownership unbundling or an Independent

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System Operator (ISO) for gas

- a more structurally challenging option than the ITO option as agreed by the Council. The ISO has to have all the assets necessary to carry out its activities without relying on the parent.

-- The Parliament wants more powers for national regulators and the proposed EU regulatory cooperation agency than the Council has agreed, more provisions on public service and in particular regarding "fuel poverty."

-- The Parliament also wants a much reduced role for the accelerated decision-making procedure known as comitology in the adoption of new network rules. (Note: In comitology the European Parliament plays a less active role. End note.)

Outlook

¶6. (SBU) Andris Kesteris, Chef de Cabinet for Energy Commissioner Piebalgs, told Econ Officer on October 21 that the Commission is not concerned by the Energy Council's agreement on the third party (aka Gazprom) clause. Under the Council version, the Commission must be consulted to determine whether the acquisition would "put at risk the security of energy supply to the Community," but its decision is only advisory. Kesteris said the Commission's opinion would be public, making it difficult for Member States to contravene. He denied rumors that Parliamentarians would seek to vest the decision-making authority with the Commission during upcoming negotiations. He expects the Parliamentarians to be more focused on pricing and consumer issues in advance of next year's elections.

¶7. (SBU) On October 21 Econ LES spoke with the head if the Parliament's ITRE Committee secretariat Luis Martin Oar and with Walter Goetz. Oar and Goetz indicated they expect negotiations with the Council on a second reading agreement to commence in early January under the Czech Presidency. They said the French had refused to commence informal negotiations, because they want to give priority to the

Climate and Energy package. According to Oar and Goetz, ITRE chair Angelika Niebler discussed this again with the French Presidency on October 21, without any success. Goetz also said that in practical terms, with negotiations on the energy and climate package going on, it would also be difficult to organize parallel negotiations on the 3rd energy package.

¶18. (SBU) To allow the Parliament the full four months of negotiating time it is entitled to under the Co-decision procedure, the Parliament will wait on the formal announcement of the Council common position in January. Oar and Goetz are optimistic that the Parliament can negotiate a deal with Council within those four months. Oar and Goetz expect Parliament's rapporteurs to be "sufficiently positive" about the Council version. They also said the ITRE Committee had a track record of agreeing to 90 percent of the legislation presented for a second reading (preventing a conciliation procedure). Both staffers expect a Parliament plenary vote on the package to take place in April or May.

¶19. (SBU) On the content of the legislation, Oar and Goetz said the Parliament would not have the necessary qualified majority to insist on mandatory ownership unbundling for the electricity market (as it did at first reading). What will probably happen is that the Parliament will concede to the council a more flexible "a la carte approach" for the electricity market (as it did for natural gas). In return, the Parliament will push for a stronger European energy authority and stronger consumer protection.

¶10. (SBU) Arana told Econ Officers that she believes the political will exists in both the Council and the Parliament to reach a compromise agreement next Spring. She believes the Parliament will be willing to accept the Council proposals on unbundling and the third country clause. She Arana believes the final version will include three options for unbundling: the full ownership unbundling proposed by the Commission, the ITO model proposed by the Council, and the ISO model proposed by the Parliament. Member states would be able to choose one of these three models. In exchange, the Parliament will likely expect concessions from the Council on a string of Parliamentary proposals for consumer protection.

Silverberg.

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